

# CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM STATEMENT OF INVESTMENT POLICY

## FOR CUSTODY MANAGEMENT

~~October 12, 2007~~ November 13, 2007

*This ~~P~~olicy is effective immediately upon adoption and supersedes all previous Custody Management Policies.*

### I. PURPOSE

The CalPERS Total Fund Statement of Investment Policy, adopted by the CalPERS Investment Committee ("Committee"), sets forth CalPERS' overarching investment purposes and objectives with respect to all its investment programs.

Pursuant to California Government Code Section 20172, the CalPERS Board has statutory authorization to "...retain a bank or trust company to serve as custodian for safekeeping, delivery, securities valuation, investment performance reporting, and other services in connection with investment of the retirement fund."

This document sets forth the policy ("Policy") for shall establish the custody of California Public Employees' Retirement System ("the System~~CalPERS~~") assets, and assures that custodians and other participants selected by CalPERS take prudent and careful action while safeguarding the standards of prudence, and service expectations ensuring that the System's~~CalPERS~~' assets are effectively safeguarded.

This Policy shall also address the responsibilities and delegations of relevant parties and shall be informative to investment managers and other interested parties whose business operations may be affected by its adoption.

### II. POLICY OBJECTIVE

This Policy shall ensure the safe, efficient, and accurate custody of the System's CalPERS' assets through a carefully planned and executed program for safekeeping, delivery, securities valuation, investment performance reporting, and other custodial services provided. This Policy shall establish the standards through which the System evaluates the effectiveness of the custody implementation. To carry out this Ppolicy, CalPERS will contract with custodial firms which have with sufficient financial strength to protect the interests of CalPERS. Contracted custodians ("Custodian") will be required, at a minimum, to demonstrate a long-term credit rating of Moody's A1 and S&P A+ (U.S. firms) or a similar measure of financial strength (non-U.S firms).

### III. RESPONSIBILITIES AND DELEGATIONS

~~A. Pursuant to California Government Code Section 20172, the System's Board has statutory authorization to "retain a bank or trust company to serve as custodian for safekeeping securities, delivery, valuation, investment performance reporting, and other custodial services in connection with investments of the retirement fund."~~

~~Pursuant to Article XVI, Section 17 of the California Constitution, the System's Board is granted plenary authority and exclusive fiduciary responsibility over the assets of the System. Through Resolution No. 92-04-B, the Board exercises its constitutional responsibility and control over the process for the procurement of all investment assets of the retirement fund. These responsibilities include the ability to delegate all or a portion of these responsibilities to Staff.~~

~~While the System's Board of Administration ("the Board") is responsible for the custody of the assets, it delegates specific responsibilities to System Staff to carry out its fiduciary responsibilities.~~

~~**B. The System's Investment Committee** ("the Investment Committee") is responsible for approving and amending the Policy. The Investment Committee delegated the responsibility for administering custody management portion of the System to the Investment Staff through the Delegation of Authority (EXE 95-101). The Investment Committee's duties include, but are not limited to, the following responsibilities:~~

- ~~1. Selecting a custodian to hold assets.~~
- ~~2. Negotiating fees and contracts.~~
- ~~3. Monitoring the delivery of services provided by its custodian.~~

~~C.A. The System's CalPERS' Investment Staff ("the Staff") is responsible for duties include, but are not limited to, the following:~~

- ~~1. Developing and recommending the Policy to the Investment Committee.~~
- ~~2. Developing and maintaining a procedures manual subject to periodic reviews and updates, outlining Staff operational procedures used in implementing this Policy.~~
- ~~3. Implementing and adhering to this Policy.~~
- ~~4. Reporting immediately to the Investment Committee all material violations of the Policy with explanations and recommendations.~~

~~5. Reporting to the Investment Committee about the performance of the custodian.~~

~~6. Reporting to the Chief Investment Officer concerning the implementation of this Policy.~~

1. Monitoring the implementation of, and compliance with, the Policy. Staff shall report concerns, problems, material changes, and all violations of the Policy immediately and in writing to the Committee. These reports shall include explanations of the violations and appropriate recommendations for corrective action.

2. Notifying Custodian in writing of the appointment, suspension, or termination of any investment manager.

8.3. Developing and recommending to the Committee the criteria and methodology to the System's Investment Committee for Custodian selection, ng the custodian consistent with Section IV. A and the System's CalPERS' enterprise-wide competitive solicitation and contracting procurement procedures.

9.4. Determining Ensuring that all other original investment documents including deeds, titles, partnerships, and insurance contracts shall be are safeguarded in a fireproof safe within accordance with the System's CalPERS' enterprise-wide Business Continuity Plan organization.

#### **IV. RESPONSIBILITIES AND CRITERIA OF THE CUSTODIAN**

A.B. The eCustodian duties include, but are not limited to, at a minimum, must meet the following criteria:

~~1. Be of global stature;~~

2. Have accounting and custodial capabilities and internal controls consistent with industry standards; and

4.3. Other criteria as determined by the System.

#### **Custodial, Accounting, and Reporting Services**

B.1. The custodian shall pProvideing the custodial, accounting and reporting services for all eligible assets held in the CalPERS' name, in a manner consistent with industry standards and subject to strict internal controls of the System. The Custodian shall provide

~~reporting services for any accounts custodied assets held by additional agents or sub-custodians appointed by the System~~CalPERS or the Custodian. These services shall be provided in accordance with, but not limited to, the following stipulations:

1.a. The eCustodian shall establish on its books and records, a separate ~~System~~CalPERS account (Account), or sub accounts for purposes determined by ~~the System~~CalPERS, consisting of all assets owned along with net asset values or market values, where applicable, and earnings, ~~or income,~~ and other cash flows related to these assets.

2.b. The eCustodian shall hold and direct its agents or sub-custodians to hold all securities and other CalPERS assets ~~of the System~~ in separate accounts or sub-accounts. The assets are not to be commingled with general assets or deposits of the eCustodian or sub-custodians, except for cash awaiting instructions or other disposition. Custodial assets are the sole property of ~~the System~~CalPERS and not general assets of the eCustodian. ~~The System~~CalPERS agrees that the securities and other CalPERS assets ~~of the System~~ may be held by the eCustodian or its sub-custodians and may be maintained by them in the securities depositories, clearing agencies, and book entry systems agreed upon.

3.c. The eCustodian shall release and deliver, or direct its agents or sub-custodians to release and deliver, CalPERS assets ~~of the System~~ upon **Proper Instructions** as ~~provided specified~~ in the ~~Staff Operations Manual~~ custodial contract, as amended from time to time.

4.d. The eCustodian shall claim any **security** they believe another institution, depository, and third party ~~lending agent~~ holds and registers in ~~the System's~~CalPERS' name.

5.e. The eCustodian shall register all of ~~the System's~~CalPERS' assets in the name of CalPERS or as required by the depository provided books and records, which are maintained by the eCustodian showing ~~System~~CalPERS ownership.

6.f. The eCustodian may open one or more cash accounts when disbursing or remitting assets in the transition process to and from the ~~System~~ CalPERS.

7.g. The eCustodian shall collect, on behalf of CalPERS, income, interest, dividends, refunds, and other proceeds accruing to securities of the ~~System~~ CalPERS, except for securities loaned by third parties.

8.h. The eCustodian shall pay out or direct its agents or sub-custodians to pay out money of the ~~System~~ CalPERS and adhere to ~~the following~~ Proper Instructions provided in the ~~Staff Operations Manual~~ custodial contract, as amended from time to time.

~~The System delegates to the custodian the discretion to appoint and remove agents or sub-custodians to assist them in carrying out its responsibilities. The custodian shall retain full responsibility and liability for selection of said entities, their actions, errors and omissions.~~

10.i. The eCustodian shall process proxies or proxy materials in accordance with the ~~System's~~ CalPERS' proxy voting policy and procedures, as amended from time to time as outlined in the Staff Operations Manual.

11.j. The eCustodian shall transmit promptly to the ~~System~~ CalPERS or the Investment Manager all written information received concerning assets held in the Fund in its custody.

12.k. The eCustodian shall keep accurate and detailed accounts of all investments, receipts, and other transactions involving the ~~System~~ CalPERS. These records shall be separate for each sub-account and include proof of all transactions involving securities held in the account. The securities shall be priced and valued by a third party pricing service ~~selected~~ approved by the System CalPERS.

13.l. The eCustodian shall process all cash movements across its books in full compliance with the state of California regulations regarding claims and remittances.

m. The Custodian shall provide assurances, through a third-party review acceptable to CalPERS, that internal controls are sufficient to protect CalPERS' assets.

14.n. The eCustodian shall provide electronic tools or systems which will enable the System's CalPERS Staff access to its workstation products on the System's Local Area Network to fulfill its duties to manage, monitor and report on investments and investment performance. ~~The custodian shall ensure that products are updated in a timely manner and released with the completion of new versions.~~

o. Upon request of CalPERS, the Custodian shall provide to designated CalPERS consultants relevant information regarding CalPERS' assets, accounting, and performance.

### **Fiduciary Relationship**

9.2. The eCustodians, sub-custodians, and agents shall acknowledge their fiduciary relationship with ~~the System~~ CalPERS. They shall discharge each of their duties therein and exercise each of their powers (as those duties and powers are defined herein), with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters uses in the conduct of an enterprise of a like character and with like aims. The eCustodian is required to contractually inform all sub-custodians and agents of this fiduciary relationship.

### **Ethics and Conflicts of Interest**

3. Custodians shall comply with CalPERS' policies and procedures, as amended from time to time, relating to ethics and conflicts of interest.

### **Custody of Assets Outside the United States**

4. The Custodian shall have a comprehensive system, acceptable to CalPERS, of selecting and evaluating sub-custodians and monitoring their internal control structures, performance and financial conditions.

## **II. CUSTODY OF ASSETS OUTSIDE THE UNITED STATES**

A.5. All sub-custodians and agents appointed by the primary eCustodian to hold assets outside the United States must comply with the responsibilities standards for of the Custodian listed in Section III.B. of this Policy and with the standards listed below for eligible foreign custodians.

B.6. Eligible foreign custodians are entities that are incorporated or organized under the laws of a country other than the United States and meet the following criteria:

1.a. Qualified foreign banks or majority-owned direct or indirect subsidiaries of U.S. banks or bank holding companies.

2.b. Securities depositories or clearing agencies that act as systems for the central handling of securities or equivalent book entries in the countries that are regulated by foreign financial regulatory authorities.

3.c. Securities depositories or clearing agencies that act as transnational systems for the central handling of securities or equivalent book entries.

~~A. The custodian is responsible for approving all sub-custodians and agents appointed by the primary custodian inside and outside the United States. The custodian's duties include, but are not limited to, the following responsibilities:~~

~~2. Approving selected sub-custodians or agents appointed by the custodian to hold assets outside the U.S.~~

~~3. Approving negotiated fees and contracts between sub-custodians or agents and the custodian where the System is responsible.~~

~~4. Monitoring the delivery of services of appointed sub-custodians or agents through written updates provided by the custodian's due diligence reports.~~

~~C. The System's Staff duties include, but are not limited to, the following responsibilities:~~

~~5. Ensuring the custodian implements and adheres to this Policy regarding custody of assets outside the U.S.~~

~~6. Reporting immediately to the Investment Committee all violations of this Policy related to custody of assets outside the U.S. with written explanations and recommendations.~~

~~7. Reporting to the Investment Committee the performance of all sub-custodians or agents appointed by the primary custodian.~~

~~8. Reporting to the Chief Investment Officer concerning the implementation of this Policy related to custody of assets outside the U.S.~~

~~B. The standards and criteria of agents or sub-custodians appointed by the custodian to safeguard assets outside the United States shall comply with the standards and criteria of the custodian written in Section IV. of this Policy.~~

## **PRUDENCE**

### **IV. ETHICS AND CONFLICTS OF INTEREST**

~~A. The custodian shall not directly or indirectly receive any benefit from recommendations made to the System. The custodian shall disclose to the System any personal investment or economic interest, which may enhance the recommendations made to the System. For further information concerning ethics and conflicts of interest, refer to Section III of the Protocol for Disclosure and Management of Potential Conflicts of Interest of Investment Consultants and Advisors for the general responsibility of consultants and advisors.~~

~~B. The custodian shall acknowledge that the System is subject to the provisions of the Fair Political Practices Laws of California and the custodian shall comply promptly with any requirement thereunder.~~

~~C. If required by law, the custodian shall require its personnel and all later substitutions therefore to file Statements of Economic Interests in compliance with the System's Conflict of Interest Code. All such reports shall be filed simultaneously with the Staff. Refer to Sections VI., VII., and VIII. in the Protocol for Disclosure and Management of Potential Conflicts of Interest of Investment Consultants and Advisors for all procedures and reporting responsibilities when a conflicts of interest have been identified.~~

### **VIII. IV. CUSTODIAN LIABILITY**

#### **Full Liability**

The eCustodian shall be fully liable for any loss to, or diminution in, the value of the Fund resulting from the eCustodian's own acts or omissions, if the resulting loss or diminution in value of the Fund is the proximate result of the eCustodian's breach of its duty of care the agreement in place as defined in the custodial contract, as amended or any other negotiated contract between the eCustodian and the System CalPERS, except when such acts or omissions are in compliance with Proper Instructions. This liability shall extend to the acts or omissions of the eCustodian's agents and sub-custodians.



~~The System~~CalPERS may, at its discretion, limit the liability of the eCustodian when doing so does not compromise the rights of ~~the System~~CalPERS or the safety or security of ~~the System's~~CalPERS' assets.

#### **IX.V. EVALUATION**

- A. Time and accuracy are of the essence for the delivery of services under this Policy. ~~The Staff Operations and Procedures Manual~~ custodial contract shall provide for the measures of the standards of service, its timeliness, and its accuracy.
- B. Each year, and at the end of the eCustodian's contract term, ~~the System~~CalPERS shall conduct an evaluation of the eCustodian's services. The evaluation shall be based on the terms outlined in the custodial contract, including but not limited to: CalPERS' satisfaction with the eCustodian's responsiveness, and the System's satisfaction with the services provided including safekeeping, transaction processing, delivery, securities valuation, investment performance reporting, and all other services in connection with the Fund.
- C. ~~An audit may be completed at any time with scope and timing solely determined by the System~~The custodial contract shall provide CalPERS with the ability to perform audits with the scope determined by CalPERS.

#### **X.VI. GLOSSARY OF TERMS**

~~Definitions for k~~Key words used in this policy are ~~located~~ defined in the ~~Miscellaneous Glossary of Terms which is included in the System's~~CalPERS' Master Glossary of Terms.

Approved by the Policy Subcommittee: May 19, 2000  
Adopted by the Investment Committee: June 19, 2000  
Revised by the Policy Subcommittee: December 10, 2004  
Approved by the Investment Committee: February 14, 2005  
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**Agent**

Individual authorized by another person, called the principal, to act in the latter's behalf in transactions involving a third party. Banks are frequently appointed by individuals to be their agents, and so authorize their employees to act on behalf of principals. Agents have three basic characteristics: 1) they act on behalf of and are subject to the control of the principal; 2) they do not have title to the principal's property; and 3) they owe the duty of obedience to the principal's orders.

**Custodian**

A bank or other financial institution that provides custody of stock certificates and other assets of an institutional investor.

**Foreign Custodian**

An entity that is incorporated or organized under the laws of a country other than the United States.

**Foreign Financial Regulatory Authority**

A governmental body or foreign equivalent of a self-regulatory organization empowered by a foreign government to administer or enforce its laws relating to the regulation of fiduciaries, trusts, commercial lending, insurance, trading in contracts of sale of a commodity for future delivery, or other instruments traded on or subject to the rules of a contract market, board of trade or foreign equivalent, or other financial activities.

**Proper Instructions**

Instructions received by the custodian from ~~the System~~CalPERS, any Investment Manager acting on CalPERS' behalf (including without limitation any securities lending agent), or any person duly authorized by either of them with respect to the pertinent asset. Such instructions may be in writing, signed by the authorized person, or may be through electronic or electro-mechanical devices, or may be through ~~such other means detailed in the custodial contract, as may be agreed to from time to time by the custodian and the party giving such instructions.~~ In addition to the above forms of instructions, the custodian may accept trade affirmations or confirmations from an institutional delivery system, such as ~~the System~~CalPERS shall certify to the custodian, and cause each Investment Manager to similarly certify, the names and specimen signatures of persons authorized to give proper instructions. The custodian shall be entitled to rely upon the identity and authority of such persons, and upon the actions taken by such persons, until it receives notice from ~~the System~~CalPERS or the Investment Manager to the contrary.

**Proxy**

Written power of attorney given by shareholders of a corporation authorizing a specific vote on their behalf at corporate meetings.

**Safekeeping**

Storage and protection of a customer's financial assets, valuables, or documents, provided as a service by an institution serving as an agent and where control is delegated by the customer, also as custodian.

**Security**

Instrument that signifies an ownership position in a corporation (stock), a creditor relationship with a corporation or governmental body (bond), or rights to ownership such as those represented by an option, subscription right, and subscription warrant.

**Sub-Custodian**

Any bank or other financial institution appointed by the master custodian to provide custody of assets within a specified region.